

**FIRST NATIONAL LIFE INSURANCE COMPANY**

**OF THE U.S.A.**

**121 South 13<sup>th</sup> Street, Suite 200**

**Lincoln, Nebraska 68508**

**Report of Examination**

**as of**

**December 31, 2009**

**State of Nebraska**

**Department of Insurance**

STATE OF NEBRASKA  
DEPARTMENT OF INSURANCE

JUN 02 2011

**FILED**

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Lincoln, Nebraska  
May 17, 2011

Honorable Bruce R. Ramge  
Director of Insurance  
State of Nebraska  
941 "O" Street, Suite 400  
Lincoln, Nebraska 68508

Sir:

Pursuant to your instructions and authorization, and in accordance with statutory requirements, an Examination has been conducted of the financial condition and business affairs of the

**FIRST NATIONAL LIFE INSURANCE COMPANY OF THE U.S.A.**  
121 South 13th Street, Suite 200  
Lincoln, Nebraska 68508

and the report of such examination is respectfully presented herein.

### **INTRODUCTION**

First National Life Insurance Company of the U.S.A., hereinafter referred to as the Company, was last examined as of December 31, 2005, by examiners of the Department of Insurance, State of Nebraska. The current financial condition examination covered the intervening period to the close of business on December 31, 2009, and includes such subsequent transactions as were considered pertinent.

## **SCOPE OF EXAMINATION**

The examination was conducted pursuant to and in accordance with both the N.A.I.C. Financial Condition Examiners Handbook and Section 44-5904(1) of the Nebraska Insurance Statutes. The Handbook requires that examiners plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. The examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and Annual Statement instructions when applicable to domestic state regulations. All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

A general review was made of the Company's operations and the manner in which its business has been conducted in order to ascertain compliance with statutory and charter provisions. Its history was traced and has been reflected in this report under the caption "Description of Company." All items pertaining to management and control were reviewed, including provisions for disclosure of conflicts of interest to the Board of Directors and the departmental organization of the Company. The Articles of Incorporation and the By-Laws were reviewed, including appropriate filings of any changes or amendments thereto. The minutes of the meetings of the shareholder and the Board of Directors, held during the examination period, were read and noted. Attendance at meetings, election of directors and officers, approval of investment transactions and

authorization of salaries were also noted.

The fidelity bond and other insurance coverages protecting the Company's property and interests were reviewed, as were the employees' and agents' welfare and pension plans. The Certificate of Authority to conduct the business of insurance in the State of Nebraska was inspected and a survey was made of the Company's general plan of operation.

Data reflecting the Company's growth during the period under review, as developed from the Company's filed annual statements for the examination period, is reflected in the financial section of this report under the caption "Body of Report."

The Company's reinsurance facilities were ascertained and noted, and have been commented upon in this report under the caption "Reinsurance." Accounting records and procedures were tested to the extent deemed necessary, including a review of internal controls. Its method of claim handling and all procedures pertaining to the adjustment and payment of incurred losses were also noted. N.A.I.C. IRIS test results were reviewed for all years covered by this examination.

The assets were verified and evaluated, and the liabilities and reserves determined as deemed necessary by the examination pre-planning process, in order to present herein a statement of the Company's financial condition as of December 31, 2009.

### **DESCRIPTION OF COMPANY**

### **HISTORY**

The Company was incorporated on March 27, 1908, and commenced business on August 8, 1908 as a burial association. The Company was originally organized as the Western Indemnity

Company. In 1937, the Company's name was changed to the First National Life Insurance Company (Limited) of the U.S.A. On August 8, 1956, the name of the Company was changed to its present form.

Effective as of January 1, 1957, the Company merged its business with that of Public Life Insurance Company, Lincoln, Nebraska, and became the surviving corporation.

In November 1978, 100% ownership of the Company was acquired by its current parent, Packers Service Group, Inc. (at that time, Packers Insurance Agency, Inc.). Effective January 1, 1979, Packers Reinsurance Company, an Arizona corporation owned by the Company's parent, was merged into the Company by means of a stock exchange.

Effective as of May 31, 2007, the Company's parent, Packers Service Group, Inc., merged its business into NelNet Academic Services, LLC, a wholly owned subsidiary of NelNet, Inc. ("NelNet").

Under the provisions of its current charter, and in conformity with Nebraska Statutes, the Company is authorized to conduct the business of a stock life insurance Company. The Amended Articles of Incorporation provide that the Company shall have perpetual existence.

## **MANAGEMENT AND CONTROL**

### **Holding Company**

The Company is a member of an insurance holding Company system as defined by Nebraska Statute. Following is a partial organizational listing flowing from the Company's parent.

NelNet, Inc.

National Education Loan Network, Inc.

NelNet Academic Services, LLC

First National Life Insurance Company of the USA (FNL)

### **Shareholder**

Article VI of the Company's Amended Articles of Incorporation authorizes the issuance of 50,000 shares of capital stock with a par value of \$10.00 per share. At the date of this examination, all of the Company's issued and outstanding shares of stock (17,500) were owned and held by NelNet, Inc. No changes have occurred in the Capital Stock and Gross Paid In and Contributed Surplus of the Company during the period covered by this examination.

Cash dividends paid since organization of the Company have totaled \$4,611,716. Dividends paid to the Company's shareholder during the examination period were as follows:

<u>Date of Payment</u>	<u>Amount</u>
June 17, 2008	\$550,000

### **Board of Directors**

The Company's Amended Articles of Incorporation provide that the affairs of the corporation shall be managed and conducted by the Board of Directors, the number of which shall be as stated in the By-Laws. The By-Laws require a Board, of not less than five nor more than twenty-one Directors, to be determined annually by the Stockholders. Directors shall be elected for a term of one year and shall serve until their successors have been elected.

Those persons serving on the Board of Directors at December 31, 2009, were as follows:

**Name and Residence****Principal Occupation**

Kenneth D. TenHulzen  
Lincoln, Nebraska

President of the Company

Frances A. Brannen  
Lincoln, Nebraska

Vice President and Treasurer  
of the Company

Jim Kruger  
Lincoln, Nebraska

Controller, NelNet, Inc.

Chuck Norris  
Lincoln, Nebraska

Director, NelNet, Inc

Todd Eicher  
Lincoln, Nebraska

Executive Director of NelNet, Inc

**Officers**

The Company's Amended Articles of Incorporation require that the principal officers shall be a President, one or more Vice Presidents, a Secretary, and a Treasurer, who shall be elected by the Board of Directors. The Officers shall serve for one year, or until their successors are elected and qualified. Officers serving the Company at December 31, 2009, were as follows:

**Name****Office**

Kenneth D. TenHulzen

President

Jay L. Dunlap

Secretary

Chuck Norris

Asst. Secretary

Frances A. Brannen

Vice President, Treasurer

James Wickham

Vice President

**Committees**

Although the Articles and By-Laws of the Company are silent regarding the establishment of committees, the Board of Directors at its September 4, 1992 meeting established an Investment



Committee. This committee has not been re-affirmed since December 17, 1999, however according to Company officials it is still active. The following individuals were serving on the committee as of December 31, 2009:

Kenneth D. TenHulzen  
Chuck Norris  
Jim Kruger

## **TRANSACTIONS WITH AFFILIATES**

### **Management Agreement**

Under the terms of an agreement between the Company and its parent, NelNet, Inc where as NelNet will provide certain consultation, assistance, advice and other resources to the Company in connection with the Company's accounting, financial planning, legal, human resources and benefits, technology and facilities needs.

In consideration of the management services furnished, the Company agrees to pay NelNet at NelNet's cost for services rendered which is subject to an annual aggregate adjustment on or before December 31 of each year.

## **TERRITORY AND PLAN OF OPERATION**

As evidenced by a current Certificate of Authority, the Company is licensed to write Life and Sickness and Accident Insurance in the State of Nebraska.

The production of business is supervised and directed by the Company's President. The primary thrust of the marketing effort is the writing of credit life and disability insurance on loans to borrowers made by banks and financial institutions. This production is generated through home

office employees working directly with approximately 769 licensed agents in 350 banks and branches.

## **REINSURANCE**

The Company's reinsurance facilities are outlined below:

### **Ceded Credit Life and Accident & Health**

An Automatic Reinsurance Agreement is in place with Munich American Reassurance Company providing automatic excess coverage of new credit life and credit A&H business written directly by the Company on or after January 1, 2000, or existing credit life business written prior thereto. Plans covered include Level Term - Single or Joint Life, Decreasing Term - Single or Joint Life, Credit - A&H and Outstanding Balance - Credit Life. The maximum amount retained by the Company per individual is: life - \$20,000, A&H - \$300 per month and outstanding balance - \$15,000. On outstanding balance business, for amounts up to \$15,000 the Company retains 100% of the risk. For amounts in excess of \$15,000 but not more than \$30,000, the entire risk is shared equally. All amounts in excess of \$30,000 will be ceded to a binding limit of \$20,000. On level and decreasing term single and joint life plans, the reinsurer will accept up to \$105,000 in excess of retention through age 65 and up to \$1,200 per month on A&H. Reinsurance premiums under this agreement are subject to an experience refund computed at the end of each calendar year. Reinsurance premiums for credit life are based on monthly renewable term, payable in advance. Credit A&H premiums are on a quota share coinsurance basis.

### Ceded Ordinary Life

An automatic coinsurance agreement with Optimum Re Insurance Company provides coverage on Universal Life plans. The total amount of automatic life coverage ceded shall be up to four (4) times the Company's retention for age and classification, up to a maximum of \$60,000 on any one life. The Company's retention is \$15,000 per life all ages and ratings. The treaty contains an automatic jumbo limit that provides that the Company shall not automatically cede any risk where the amount in force would exceed \$2,000,000 on any one individual. The minimum amount of insurance ceded shall not be less than \$2,000. The treaty allows for facultative options. Life and accidental death benefits under this agreement are on a Yearly Renewable Term basis and rate. The treaty contains a production/persistency bonus on the in-force business. Coverage includes both standard and substandard lives, accidental death benefits, and waiver of premium disability benefits.

An automatic coinsurance agreement with Optimum Re Insurance Company provides coverage on business referred to as the Annual Renewable Term - "ART 100" Plan. The treaty provides for automatic cessions not to exceed four (4) times the Company's maximum retention of \$15,000 for all ages. The treaty contains an automatic jumbo limit that provides that the Company shall not automatically cede any risk where the amount in force would exceed \$2,000,000 on any one individual. The minimum amount of insurance ceded shall not be less than \$2,000. The treaty allows for facultative options. Life and accidental death benefits under this agreement are on a Yearly Renewable Term basis and rate. The treaty contains a production/persistency bonus on the in-force business. Coverage includes both standard and

substandard lives, accidental death benefits, and waiver of premium disability benefits.

An automatic bulk accidental death agreement, referred to as agreement No. 3415, with Swiss Re Life & Health America, Inc. covers all accidental death risks on either a standard or substandard basis when issued as a supplementary benefit to a life insurance policy. The maximum amount on any one life that may be ceded shall not exceed \$200,000. The treaty provides for facultative options. This agreement is in run-off status.

A Simplematic Individual Excess (SIE) agreement with Swiss Re Life & Health America, Inc. is in run-off with limited renewal business remaining. This is an automatic excess treaty on standard and substandard lives ceded on a YRT basis. Jumbo limits include \$3,500,000 ages 0 – 60, and \$2,000,000 ages 61 –65. The minimum risk reinsured was not less than \$5,000 or 10% of the initial face amount of any policy issued.

The Company has an agreement covering life, waiver of premium disability and ADD benefits with Ameritas Life Insurance Corporation that is in run-off.

The Company has an agreement with Lincoln National Life Insurance Company covering life benefits in excess of \$10,000, waiver of premium disability and double indemnity. This agreement is in run-off status.

#### General

All reinsurance contracts reviewed were found to contain the usual provisions relating to insolvency and termination.

## **BODY OF REPORT**

### **GROWTH**

The following comparative data reflects the growth of the Company during the four-year period under review:

	<b><u>2006</u></b>	<b><u>2007</u></b>	<b><u>2008</u></b>	<b><u>2009</u></b>
Admitted assets	\$6,376,904	\$6,898,780	\$5,349,696	\$5,419,255
Aggregate life reserves	2,860,884	2,907,252	2,406,116	2,428,543
Aggregate A&H reserves	1,442,935	1,468,274	1,497,633	1,394,438
Total liabilities	4,758,616	4,831,974	4,201,025	4,160,336
Unassigned funds	1,328,425	1,776,943	858,808	969,056
Premiums earned	1,820,862	1,675,062	1,628,222	1,422,726
Net investment income	149,949	153,256	135,872	177,463
Net income	(28,023)	408,330	(64,541)	(24,870)
Life insurance in force *	80,522	81,196	80,566	76,125

\*(000 omitted)

### **FINANCIAL STATEMENTS**

The following statement of admitted assets and liabilities, together with the accompanying summary of operations, reflect the financial condition of the Company at December 31, 2009, and its transactions for the year 2009, as determined through this examination. A reconciliation of the capital and surplus account for the period under review is also included:

## **FINANCIAL STATEMENT**

**December 31, 2009**

<b><u>Assets</u></b>	<b><u>Assets</u></b>	<b><u>Assets Not Admitted</u></b>	<b><u>Net Admitted Assets</u></b>
Bonds	\$2,990,078		\$2,990,078
Common stocks	1,338,051		1,338,051
Cash and short term investments	800,944		800,944
Contract loans	<u>8,854</u>		<u>8,854</u>
Subtotals, cash and invested assets	\$5,137,927		\$5,137,927
Investment income due and accrued	23,376		23,376
Uncollected premiums	121,856		121,856
Deferred premiums	3,763		3,763
Amounts recoverable from reinsurers	4,511		4,511
Current federal and foreign tax Recoverable	13,664		13,664
EDP equipment	1,590	\$564	1,026
Receivables from Parent	<u>113,132</u>	<u>      </u>	<u>113,132</u>
Totals	<u>\$5,419,819</u>	<u>\$564</u>	<u>\$5,419,255</u>

**Liabilities, Surplus and Other Funds**

Aggregate reserve for life policies and contracts	\$2,428,543
Aggregate reserve for accident and health policies	1,394,438
Contract claims:	
Life	41,308
Accident and health	28,024
Other amounts payable on reinsurance	26,883
Interest maintenance reserve	426
General expenses due or accrued	1,230
Taxes, licenses and fees due or accrued	(1,419)
Current federal and foreign income taxes	2,129
Net deferred tax liability	78,428
Unearned investment income	164
Amounts held for agents' account	151
Remittances and items not allocated	8,169
Asset valuation reserve	150,410
Maturities payable	<u>1,452</u>
 Total liabilities	 <u>\$4,160,336</u>
 Common capital stock	 \$ 175,000
Gross paid in and contributed surplus	114,863
Unassigned funds (surplus)	<u>969,056</u>
 Total capital and surplus	 <u>\$1,258,919</u>
 Total	 <u>\$5,419,255</u>

### SUMMARY OF OPERATIONS - 2009

Premiums and annuity considerations	\$ 1,422,724
Net investment income	177,463
Amortization of interest maintenance reserve	2,111
Commissions and allowances on reinsurance ceded	<u>185,622</u>
Total	<u>\$ 1,787,920</u>
Death benefits	\$ 332,007
Disability benefits and benefits under accident and health policies	261,907
Surrender benefits	14,603
Increase in aggregate reserves for life and accident and health policies	<u>(80,767)</u>
Subtotal	\$ 527,750
Commissions on premium and annuity considerations	568,587
General insurance expenses	679,287
Insurance taxes, licenses and fees	57,159
Increase loading on deferred and uncollected premiums	323
Total	<u>\$ 1,833,106</u>
Net gain from operations before federal income taxes	\$ (45,186)
Federal income taxes incurred	<u>(11,136)</u>
Net gain from operations before realized capital gains	\$ (34,050)
Net realized capital gains or (losses)	<u>9,179</u>
Net income	<u><u>\$ (24,871)</u></u>



### **CAPITAL AND SURPLUS ACCOUNT**

	<b><u>2006</u></b>	<b><u>2007</u></b>	<b><u>2008</u></b>	<b><u>2009</u></b>
Capital and surplus, beginning of year	<u>\$1,592,804</u>	<u>\$ 1,618,290</u>	<u>\$2,066,807</u>	<u>\$1,148,671</u>
Net income	\$ (28,023)	\$ 408,330	\$ (64,541)	\$ (24,870)
Change in unrealized capital gains or (losses)	148,488	(50,238)	(396,364)	210,602
Change in net deferred income tax	(51,506)	15,843	52,580	(51,514)
Change in non-admitted assets	(35,119)	85,407	310	3,301
Change in asset valuation reserve	(8,354)	(10,825)	39,879	(27,270)
Dividends to stockholder	\$ _____	\$ _____	\$ (550,000)	\$ _____
Net change for year	<u>\$ 25,486</u>	<u>\$ 448,517</u>	<u>\$ (918,136)</u>	<u>\$ 110,249</u>
Capital and surplus, end of year	<u>\$1,618,290</u>	<u>\$ 2,066,807</u>	<u>\$1,148,671</u>	<u>\$1,258,920</u>

### **EXAMINATION CHANGES IN FINANCIAL STATEMENTS**

Unassigned funds (surplus) in the amount of \$969,056, as reported in the Company's 2009 Annual Statement has been accepted for purposes of this examination.

### **COMPLIANCE WITH PREVIOUS EXAMINATION RECOMMENDATIONS**

The recommendation contained in the previous report of examination is reflected below together with the remedial action taken by the Company.

**Fidelity Bond Coverage** – The Company is currently protected by \$10,000 of employee dishonesty coverage through its property insurance policy. This coverage does not appear to be adequate for the size of the Company. It is recommended that the Company review the adequacy of its current coverage.

**Action:** The Company has complied.

## **COMMENTARY ON CURRENT EXAMINATION FINDINGS**

The following comments and recommendations have been made as a result of this examination:

### **Annual Board Meetings**

During the review of the Company's By-Laws it was noted that the Company had not amended Article III, Section 1, which states the regular annual meeting of the stockholders shall be held in conjunction with the annual stockholders meeting of the Packers Service Group, Inc., who is no longer the Company's parent. It is recommended that the Company amend its Bylaws to reflect the holding of the annual stockholder meeting in conjunction with the annual stockholders meeting of NelNet Inc.

### **Investment Expense Allocation**

According to Neb. Rev. Stat. §44-322 (a)(ii), "the financial statement shall be prepared in accordance with annual statement instructions and accounting practices and procedures manuals as prescribed by the director which conform substantially to the annual statement instructions and the Accounting Practices and Procedures Manuals adopted by the National Association of Insurance Commissioners."

The Company is currently allocating a percentage of general expenses to investment expenses. It appears that the Company is not in compliance with the NAIC Annual Statement Instructions Section E, standards and rules for allocation of receipts and expenses in regards to the allocation of investment expenses. Per Section E, "only such methods that will produce a suitable and equitable distribution of receipts and expenses by line of business," should be used by the

Company. In addition, detail should be maintained by the Company to show the system used for allocation of expenses and the actual base of allocation.

It is recommended that the Company comply with Neb. Rev. Stat. §44-322 (a)(ii) and the NAIC Annual Statement Instructions, Section E by using a suitable and equitable distribution of investment expenses and maintain detailed records showing the system used for allocation of expenses and the actual base of allocation.

### **Board of Directors**

During our review of the Board of Directors it was noted that all five Directors were either employees of the Company or the Company's parent, NelNet Inc. It appears that the Company is not in compliance with Neb. Rev. Stat. §44-211 which states at least one-fifth of the Board of Directors shall be persons who are not officers or employees of such Company.

It is recommended that the Company comply with Neb. Rev. Stat. §44-211 by ensuring at least one-fifth of the Board of Directors are neither an officer nor employee of neither the Company nor its Parent NelNet Inc.

### **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

The following recommendation has been made as a result of this examination:

**Annual Board Meetings** - It is recommended that the Company amend its By-Laws with to reflect holding the annual stockholder meeting in conjunction with the annual stockholder meeting of NelNet Inc.

**Investment Expense Allocation** - It is recommend that the Company comply with to Neb. Rev. Stat. §44-322 (a)(ii) and the NAIC Annual Statement Instructions, Section E by using a suitable and equitable distribution of investment expenses and maintain detailed records showing the system used for allocation of expenses and the actual base of allocation.

**Board of Directors** - It is recommended that the Company comply with Neb. Rev. Stat. §44-211 ensuring at least one-fifth of the Board of Directors whom are neither an officer nor employee of neither the Company nor the Parent, NelNet Inc.

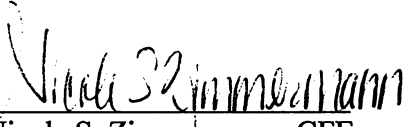
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### **ACKNOWLEDGEMENT**

The courtesy and cooperation extended by the officers and employees of the Company during the course of this examination is hereby acknowledged.

In addition to the undersigned, Linda K. Scholl, CFE, Derek J. Petersen, Examiner, William R. Schmid, Information Systems Examiner and Jeanne M. Daharsh, FSA, MAAA, Actuarial Examiner, all with the Nebraska Department of Insurance, participated in this examination and assisted in the preparation of this report.

Respectfully submitted,

  
Nicole S. Zimmermann, CFE  
Financial Examiner  
Department of Insurance  
State of Nebraska